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SUBJECT: Russian Companies: Emerging Global Players

Summary

¶1. (SBU) Russian companies are increasingly going "global" -- expanding rapidly overseas through acquisitions and investments. Russian companies, flush with cash, are joining their Indian and Chinese counterparts as a new breed of multinationals. Oil and gas companies are the most active but metals and telecommunications firms are becoming more involved abroad as well. The focus is no longer just in the CIS and Europe, but also increasingly in Asia, Africa, and to a lesser extent even in North America. These firm's motivations include the need to acquire greater technical know-how, to expand their profit base, and to take advantage of opportunities for quick returns. Presidential-hopeful Dmitry Medvedev and other Russian political leaders, no longer concerned about capital flight, have expressed support for continued foreign investment by Russian firms. End Summary

An Emerging New Player in the Global Marketplace

¶2. (U) Russian companies are increasing their participation in the global economy. They are rapidly expanding overseas investment. According to the Russian State Statistics Office (RosStat), Russia's foreign direct investment (FDI) abroad for the first nine months of 2007 exceeded \$28 billion. This compares to \$14 billion for the whole of 2006. UNCTAD'S World Investment Report shows that the stock of Russian FDI grew nearly eightfold since 2002, increasing from a starting point of \$20 billion to \$157 billion in 2007. Among emerging markets, which now account for around 14% of FDI, Russia is one of the three biggest investors along with China and Brazil.

Energy and more

¶3. (U) The most significant Russian investors abroad are Gazprom and Lukoil. Gazprom has been aggressively buying up assets in Europe and the former Soviet states and has recently expanded its efforts to include Africa. Lukoil's international presence includes projects in the Middle East, Africa, and Latin America. Other Russian energy firms, such as TNK-BP and Rosneft are also active abroad, especially in the former Soviet states.

¶4. (U) However, while energy firms are still the big players, other industries are increasing their foreign activities. According to a recent study from the Skolkovo Moscow School of Management in December 2007, 47% of the overseas assets of the top 25 Russian non-financial multinationals are from non-energy sectors: 25% from metals and mining and 22% from transport/shipping, telecommunications, and retail. The biggest metals investors were Evraz, Severstal, Norilsk Nickel, and Rusal. The largest telecommunications investors are Vimpelcom and Sistema.

No longer just CIS and Europe

¶5. (U) As to be expected based on geographic and historic ties, over 60% of the foreign affiliates of Russia's multinationals are concentrated in Europe and the CIS. However, investments in Africa, Asia and North America are growing.

¶6. (U) In Africa, four Russian mining companies: Norilsk Nickel, Rusal, Russia's diamond monopoly Alrosa, and Renova, have invested more than \$5 billion in the past three years. This February, Rusal joined with China Power Investment Corp to build a bauxite and alumina complex in Guinea, where Rusal already owns a mining firm, a refinery, and a bauxite deposit. Rusal bought a majority share in Alscon (Aluminum Smelter Company of Nigeria) last year and its smelter will start operations this month. Renova is active in South African manganese via the joint venture United Manganese of Kalahari (UMK).

¶7. (U) In Asia, telecommunications investments predominate. In September 2007, a Russian telecom company, Vimpelcom, announced plans for a global system for mobile communications based in Vietnam, possibly investing up to \$1 billion over the next few years. Vimpelcom is controlled by another Russian firm Altimco (itself part

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of the Alfa Group), which in August 2007 acquired 90% of the Cambodian mobile operator Sotelco. Sistema gained a foothold in India's fast-growing telecom market by investing \$520 million in its Indian subsidiary Shyam Telelink in 2008, and plans an additional \$7 billion in network infrastructure.

¶8. (U) Russian FDI in the United States for the first nine months of 2007 was around \$750 million (RosStat figure), a 30% increase over 2006. The top 25 Russian multinationals now have 9% of their affiliates in the United States and Canada. Much of Russia's outward FDI into the United States has been through merger and acquisitions in 2006-2007, including the purchase by Russia's biggest steelmaker, Evraz Group, of three US-based companies in 2006-2008: Stratcor, Claymont Steel Holdings, and Oregon Steel Mills. Another Russian steel producer, Severstal, purchased Rouge Industries three years ago. In Canada, Norilsk Nickel bought LionOre last year.

Motivations

¶9. (SBU) The principal motivation is, of course, profits. The ruble's appreciation vis-à-vis major currencies -- 19% against the dollar in a 12-month period, 4% against the Euro -- has given the large Russian companies spare cash to invest overseas and the chance to acquire profitable foreign companies at a discount. Russian companies are also eager to take advantage of "get-rich-quick" opportunities. Alexander Bulygin, Rusal CEO, said that the past two years were of particular importance for Rusal, which achieved "significant production and financial" results by acquiring strategic assets abroad.

¶10. (SBU) In addition, Russian companies are facing an increasingly saturated domestic market and need to expand abroad to maintain and increase profits. A telecoms analyst at J'son & Partners noted that although the domestic telecom market brought in \$20 billion in revenue in 2007, growth was the result of old clients acquiring new handsets rather than the firms acquiring new clients. In that

regard, Alexander Goncharuk, Sistema's president and CEO, recently called India one of the most attractive telecommunications markets, and one with a high growth potential. Sistema plans to build a national telecommunications network in India.

¶11. (U) A third motivation is to acquire needed technical expertise through overseas acquisitions. For instance, the Evraz Group recently acquired Oregon Steel and Claymont Steel and is using the expertise acquired in these deals to press forward with its strategy of turning itself from a Russian into a global steel producer. At the same time, they are using Russian capital to revitalize the U.S. steel plants they acquired.

Support From Above

¶12. (SBU) Russian expansion overseas is still a relatively new phenomenon, and until recently, few Russian politicians identified it as a priority. That seems to be changing. Speaking before the all-Russia Forum of Industrialists and Entrepreneurs on January 31, First Deputy Prime Minister and presidential hopeful Dmitry Medvedev expressed support for Russian companies investing abroad. Previously the government had been neutral regarding Russian investment abroad, analysts at Skolkovo Research Center in Moscow told us. Officials were concerned about capital flight and until 2006, when capital controls were lifted, Russia was a net exporter of capital.

Comment

¶13. (SBU) Despite global aspirations, few, if any, Russian companies are expected to be market leaders any time soon. However, as long as the ruble stays strong vis-`-vis major currencies, and Russian companies remain relatively cash-rich, Russian foreign investment will continue. End Comment.

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